

Office of the Legislative Auditor

State of Montana



Report to the Legislature

December 1989

Financial-Compliance Audit

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Department of Highways

For the Two Fiscal Years Ended June 30, 1989

This report contains recommendations in the following areas:

- ▶ Lack of Internal Control Documentation
- ▶ Unauthorized Disposal of Scrap Metal
- ▶ Limited Communication Between District Offices

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FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Office of the Legislative Auditor to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations which could have a significant financial impact. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

The Single Audit Act of 1984 and OMB Circular A-128 require the auditor to issue certain financial, internal control, and compliance reports regarding the state's federal financial assistance programs, including all findings of noncompliance and questioned costs. This individual agency audit report is not intended to comply with the Single Audit Act of 1984 or OMB Circular A-128 and is therefore not intended for distribution to federal grantor agencies. The Office of the Legislative Auditor issues a statewide biennial Single Audit Report which complies with the reporting requirements listed above. The Single Audit Report for the two fiscal years ended June 30, 1987 has been issued. Copies of the Single Audit Report can be obtained by contacting:

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STATE OF MONTANA

Office of the Legislative Auditor

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LEGISLATIVE AUDITOR:
SCOTT A. SEACAT

LEGAL COUNSEL:
JOHN W. NORTHEY

December 1989

DEPUTY LEGISLATIVE AUDITORS:

MARY BRYSON
Operations and EDP Audit

JAMES GILLET
Financial-Compliance Audit

JIM PELLEGRINI
Performance Audit

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Highways' financial activity for fiscal years 1987-88 and 1988-89. The department's written response to audit recommendations is included in the back of the report.

We thank the director and department staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

Scott A. Seacat
Legislative Auditor

Department of Highways

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 1989

Members of the audit staff involved in this audit were Mark Barry, Jeane Carstensen, Renee Foster, Wayne Kedish, Rich McRae, Jill Olson, Cindy Susott, and Gary Trescott.

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Appointive and Administrative Officials

			Term <u>Expires</u>
Montana Highway Commission	Dan Huestis, Chairman	Great Falls	1993
	Gerald Archambeault	Glasgow	1991
	Tom Conroy	Hardin	1993
	Roy Duff	Whitefish	1991
	Dennis Shea	Butte	1993
Department of Highways			
Administrative Officials	Larry Larsen, Director		
	Robert Champion, Deputy Director (Acting)		
	William Salisbury, Administrator Centralized Services Division		
	Thomas Barnard, Administrator Engineering Division		
	David Galt, Administrator (Acting) Gross Vehicle Weight Division		
	James Beck, Administrator Legal Division		
	Donald Gruel, Administrator Maintenance & Equipment Division		
	Russell McDonald, Administrator Personnel Division		
	Steve Kologi, Administrator (Acting) Program Development Division		
	District Engineers		
	Roy R. Ventura, Jr. - Billings		
	Kenneth G. Rapp - Butte		
	Bruce Russell - Glendive		
	Eugene M. Stettler - Great Falls		
	James T. Weaver - Missoula		

Summary of Recommendations

The listing below serves as a means of summarizing the recommendations contained in the report, the department's response thereto, and a reference to the supporting comments.

Recommendation #1

We recommend the department:

- A. Implement policies requiring review and approval of project estimates and equipment usage reports; and 8

Agency Response: Concur. See page 23.

- B. Implement procedures to ensure all equipment usage charged to federal projects is adequately supported. 8

Agency Response: Concur. See page 23.

Recommendation #2

We recommend the department implement procedures to ensure disposal of scrap metal and recording of related revenue and expenditures are in compliance with state law and policy. 9

Agency Response: Concur. See page 24.

Recommendation #3

We recommend the department encourage periodic meetings among the district centralized services supervisors. 11

Agency Response: Concur. See page 24.

Introduction

Introduction

We performed a financial-compliance audit of the Montana Department of Highways for the two fiscal years ended June 30, 1989. The objectives of the audit were to determine:

1. The department's compliance with applicable federal and state laws and regulations.
2. If the financial schedules present fairly the changes in fund balance and results of operations of the department for the two fiscal years ended June 30, 1989.
3. The effectiveness of administrative and accounting controls used to ensure resource use is consistent with laws and regulations; resources are safeguarded against waste, loss and misuse; and reliable information is maintained and fairly disclosed in the financial records.
4. The implementation status of prior audit recommendations.

This report contains three recommendations to the department. These recommendations address areas where management, internal control, and compliance with laws and regulations can be improved. Other areas of concern deemed not to have a significant effect on the successful operations of the department programs are not specifically included in the report but have been discussed with management.

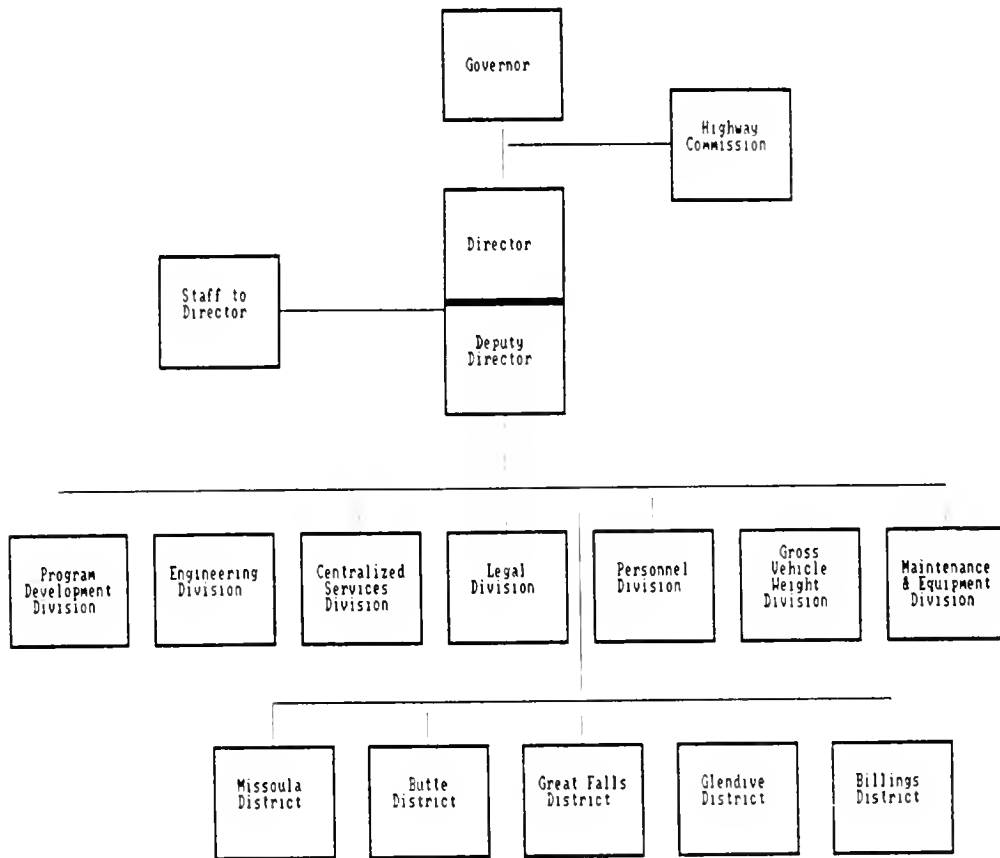
In accordance with section 5-13-307, MCA, we analyzed the costs of implementing the recommendations made in this report. Each report section discloses the cost, if significant, of implementing the recommendation.

General

The department is responsible for the planning, layout, construction, improvement, repair, and maintenance of state highways and federal aid system highways. The department's responsibilities also include the collection of fees and enforcement of laws related to the Gross Vehicle Weight regulations.

The department is an executive branch agency and is organized as follows:

Introduction



Source: Department of Highways

The Department of Highways is under the direction of the Highway Commission and the director. The Highway Commission is composed of five members appointed by the governor for four year terms with Senate confirmation. The commission determines construction priorities, selects construction projects, and determines the allocation of financial aid. It also classifies highways as federal aid highways, primary highways, and/or off-system highways in the state maintenance system. The commission may delegate certain functions to the director of the Department of Highways. The director is appointed by the governor and confirmed by the Senate.

Introduction

The department employed 1,921 full-time equivalent employees (FTE) at June 30, 1988 and 1,931 FTE at June 30, 1989.

Budgeted expenditures and transfers out were \$273,397,289 in fiscal year 1987-88 and \$285,601,062 in fiscal year 1988-89. The expenditures were grouped by program in the appropriation legislation and are summarized by program in the Schedule of Budgeted Expenditures and Transfers Out by Program and Fund in the financial schedules attached to this report, see pages 16 through 17. The budgeted programs and the management divisions they relate to are:

General Operations Program - provides the overall administrative support services essential to the operations of the department through the Director's Office, and the Centralized Services, Program Development, and Personnel Divisions.

Construction Program - is responsible for ensuring that roads and bridges are constructed or reconstructed to appropriate design standards. It supervises highway construction from project award through completion and approval of the project. These services are generally provided through the Engineering Division.

Maintenance Program - is responsible for preserving and repairing all highways and their appurtenances within the right-of-way of interstate, urban, primary, and state-maintained secondary highway systems in Montana. These services are generally provided through the Maintenance and Equipment Division.

Preconstruction Program - carries out the planning stages of highway development, including determining location and design, conducting any necessary public hearings, acquiring needed rights-of-way, and processing highway projects for contract award through the Engineering Division.

Highway Service Revolving Program - provides certain support services (such as data processing, printing, photography, airplane, and material testing) common to all divisions within the department. Currently, these services are billed to the user divisions based on the amount of use. Beginning in fiscal year 1989-90 this program will be eliminated and the activities administered under the general operations and equipment programs.

Introduction

State Motor Pool Program - operates and maintains a fleet of rental vehicles available to all state officials and employees in the Helena area to facilitate the conduct of official business. The service operates under the Maintenance and Equipment Division. Cost of services is recovered through user fees.

Equipment Program - is responsible for the purchase and maintenance of a fleet of equipment and vehicles for use within the Department of Highways. The primary goal is to provide replacement equipment and maintain and repair existing equipment in a cost effective manner. The Maintenance and Equipment Division administers this program. Costs are recovered through user fees.

Interfund Transfers Program - this program is used to record transfers to the Reconstruction Trust Fund and Highway Bond Debt Service Funds and is administered by the Centralized Services Division. This program was the "Capital Outlay" program in prior fiscal years.

Stores Inventory Program - purchases and stores materials (such as sand, road oil, and gasoline) needed by other programs within the department. Centralized Services Division administers this program.

Bonds Program - includes activity related to the principal and interest on the \$150,000,000 in Highway Revenue Bonds and \$7,300,000 in Highway Building Complex bonds outstanding during the audit period. This program was established in fiscal year 1988-89. This program is administered by Centralized Services Division.

Gross Vehicle Weight Program - provides enforcement of the statutes and regulations relating to vehicle weights on the state's highways (Title 61, MCA) and collects gross vehicle weight fees. This program is administered by Gross Vehicle Weight Division.

Prior Audit Recommendations

Prior Audit Recommendations

The previous audit for fiscal years 1985-86 and 1986-87 contained six recommendations still applicable to the department. The department has implemented five of the recommendations and not implemented the other. The recommendation that was not implemented relates to documentation of internal controls and is discussed on pages 6 to 8.

Findings and Recommendations

Internal Controls

The department receives Federal Highways Planning and Construction Grant (CFDA #20.205) moneys to aid in the construction of federal aid highways. During our examination in the last audit, we noted two instances where documentation of the existence of internal controls related to this grant was lacking. Our follow-up indicated documentation has not significantly improved.

Documentation of Project Estimate Controls

Major highway construction projects are supervised by a field project manager. The field project manager is responsible for preparing a project estimate, which is used to generate payments to contractors for the work completed. We identified the field project manager's review and approval of the completed project estimate as one of the key controls in the contractor claims section of the expenditure cycle. Our testing, in the last audit, disclosed that the field project manager was no longer signing the project estimate as evidence of the control.

Our current audit testing indicates the department has not established a uniform policy requiring project managers to review and approve the progress estimates used for payments to contractors. We interviewed and/or examined workpapers from 17 field project managers. Ten of the field project managers involved were not aware of the policy. As a result we could not conclude the prior audit recommendation had been implemented.

Project estimate information is submitted by the field project manager through a series of verbal, manual, and/or electronic processes. There is a potential for errors to occur at each stage of the processing. Since the field project manager is on site at the project and is the one preparing the original estimate, the field project manager is the individual with the best opportunity to compare input to output and detect errors in a timely manner. If errors occur and are not detected in a timely manner they could result in overpayments to contractors that may not be detected for several years.

Findings and Recommendations

Department personnel indicated this control was overlooked when a major change in the project estimate system was implemented. Since our last audit the attempts to implement this control had been on a district by district basis. The district by district approach resulted in less than complete implementation of this control. It appeared the department did not emphasize the importance of this review and approval control. Department personnel indicated increased emphasis will be placed on this control in the future.

Documentation of Equipment Usage Report Controls and Questioned Costs

The department's equipment management system does not ensure all equipment usage reports are reviewed and approved. The department uses the system to develop management information and bill projects for equipment use. The input for this system is an equipment usage report, prepared by the operator of the equipment, detailing what projects should be charged for the equipment's use. Department policy requires supervisors review and initial reports to indicate the approval of charges to the various projects. This review and approval is designed to ensure accurate charges to projects on which the equipment was used.

Our sample testing, of fiscal years 1987-88 and 1988-89 transactions, at department headquarters, revealed 15 equipment usage reports out of 103 tested that were not signed by the supervisors. We also found 5 equipment usage reports out of the 103 that could not be adequately supported by the department as federal project charges. Two of the five were not signed as approved by the supervisor. These five items resulted in our questioning \$244 of costs charged to federal projects. Department personnel indicated equipment usage charged to federal projects for all districts amounted to \$711,654 and \$782,390 in fiscal years 1987-88 and 1988-89 respectively. We followed up on the results of our sample at all five district offices. We found if signatures were present on the equipment usage reports (less than 50 percent were signed at most districts) they often were signed by office or supervisory personnel who had little or no knowledge of the accuracy of the information on the usage report.

Findings and Recommendations

Department personnel indicated the lack of signatures was due to confusion over which supervisor should approve the reports and what the review should include. They also indicated that new emphasis will be given to this control in the future.

Recommendation #1

We recommend the department:

- A. Implement policies requiring review and approval of project estimates and equipment usage reports; and**
- B. Implement procedures to ensure all equipment usage charged to federal projects is adequately supported.**

State Compliance

Scrap Metal Disposal

Procedures, at the district and division offices, for disposing of scrap metal are not in compliance with state law and policy. Each of the districts and divisions accumulate and recycle scrap metal. The scrap metal results primarily from equipment maintenance and repair, unsalvageable signs, and metal objects cleared from road ways. Two areas of state law/policy are involved, appropriations and surplus property.

Three of the department's five districts were taking the scrap metal to dealers and obtaining credit memos and then charging the purchase of new metal against the credit. This method of bartering for goods or services avoids the appropriation process by not recording actual revenues and expenditures. State law requires all revenue and expenditure be recorded on the accounting records. We estimate \$1,000 to \$2,000, per fiscal year, of revenue and related expenditures at each of three districts were not recorded on the department's accounting records. It was not cost effective to determine the exact amount of unrecorded revenue or expenditures due to differences in the

Findings and Recommendations

level of documentation.

Disposal of scrap metal falls under the heading of surplus property. State policy states "Department of Administration (DofA) has exclusive power . . . to authorize the sale or other disposition of, all materials and supplies, service equipment or other personal property of every kind owned by the state . . ." The Department of Highways could not produce documentation of authorization, from DofA, for the disposal of scrap metal.

Department personnel indicated a disposal authorization was assumed to exist but no record could be found. Personnel also indicated the barter method of disposal was the result of no written department policy on the subject. We notified the department of this finding. The department has since obtained authorization from DofA to dispose of scrap metal and has issued a draft department policy that, when implemented, will comply with state law.

Recommendation #2

We recommend the department implement procedures to ensure disposal of scrap metal and recording of related revenue and expenditures are in compliance with state law and policy.

District Office Communication

During our review of district office procedures we noted a wide variety of methods used by the districts to accomplish similar tasks. The methods also varied in economy and effectiveness between districts. Areas where we noted particularly diverse methods include:

- utility bill tracking and payments;
- computer terminal location and availability;
- stockroom controls, location, and organization;

Findings and Recommendations

- scrap metal collection and disposal; and
- used inventory identification and storage.

A more detailed explanation of the areas mentioned above will demonstrate the varied methods, economy, and effectiveness.

Utility bills - One district has developed a system of accumulating its power bills (approximately 550 per month from 16 utility companies); generating a listing of the amounts paid for each power bill; and generating all of the district's project cost coding entries for the department's accounting system.

Employees using this microcomputer based system indicate it saves forty to sixty hours of work each month tracking utility bills and has virtually eliminated duplicate payments of utility bills. One other district indicated it is considering implementing this system.

Another district implemented a utility inventory system to ensure it only pays for street lights and utilities actually used. This system provides reports from maintenance personnel regarding damaged or nonworking utility units by location and number. This system ensures timely notification of the power company for repair or, in certain cases, adjustment of charges for nonworking items. Only one other district indicated awareness of this system.

Computer terminals - Two districts had improved access to computer terminals by placing work stations on the desks of employees that used them. The employees at the districts that had improved access were using the machines to improve their efficiency. The remaining three districts still had the work stations isolated to a few locations shared by all employees or had one employee assigned to the work station. As a result of a lack of familiarity with computers, many of the employees at other districts were apprehensive about the prospects of using computers when increased computerization comes to their district.

Stockroom controls - Physical controls over stockroom and tool inventories varied widely. The extremes were one district that had excellent security, down to printing the outlines of the tools on the wall where they were stored to make finding tools easier, and one district that essentially had no physical security over the stockroom. The remaining three districts' controls covered the range between the two extremes.

Scrap metal - Methods of collecting and disposing of scrap metal varied widely. One district has different containers for collection of different types of metal. When the containers are

Findings and Recommendations

full they are taken to the scrap metal dealer and the contents are sold. Another district throws all scrap in a pile in the yard and when the pile is large enough it must be sorted, loaded in trucks, and hauled to the scrap metal dealer for sale. Two districts received payment for the scrap metal and recorded revenue on the accounting records. The other three were bartering the scrap metal sold for new metal (as mentioned in the previous section of this report).

Used inventory - The quantity and quality of used inventory varied from district to district. One district had piles of used bridge timbers, culverts and storm sewer pipe (much of it in unusable condition). Other districts had little or no used inventory. Used inventory in good condition and wisely stored can save the state money, but used inventory in poor condition stored haphazardly can cost money in lost time, inventorying, and sorting.

We noted these examples of areas where a particular district has implemented a solution to a problem or a more efficient way of accomplishing a task while performing a two day review at each district. A more detailed examination may have disclosed more examples.

Our review indicated the wide variety of methods and the resulting differences in economy and efficiency result from limited, or in some instances, a lack of communication among the supervisors of the centralized services (CSD) functions at the district level. District personnel indicated CSD supervisors meet during training sessions and seminars at department headquarters. The headquarters meetings leave little time for individuals from the districts to solve problems common to some or all districts and the format and location does not allow CSD supervisors to share ideas through direct observation. District Centralized Services officials indicated a willingness to share and exchange ideas with their counterparts in the other districts. Periodic meetings for the CSD supervisors and headquarters CSD personnel on a rotating basis at each district office would encourage communication and sharing of problems and solutions among the districts. Opportunity for economy and efficiency improvements would also be increased.

Recommendation #3

We recommend the department encourage periodic meetings among the district centralized services supervisors.

INDEPENDENT AUDITOR'S REPORT
AND
AGENCY FINANCIAL SCHEDULES

Summary of Independent Auditor's Report

Summary of Independent Auditor's Report

The auditor's opinion issued in this report is intended to convey to the reader of the financial schedules the degree of reliance that can be placed on the amounts presented. All schedules were prepared from the Statewide Budgeting and Accounting System (SBAS), without adjustment. The departments' financial schedules for the two fiscal years ending 1987-88 and 1988-89 are fairly stated in all material respects and the user of this SBAS information can rely on the information presented.

Office of the Legislative Auditor

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LEGAL COUNSEL:
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DEPUTY LEGISLATIVE AUDITORS:

MARY BRYSON
Operations and EDP Audit

JAMES GILLET
Financial-Compliance Audit

JIM PELLEGRINI
Performance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying financial schedules of the Department of Highways for each of the two years ending June 30, 1988 and 1989, as shown on pages 14 through 21. The information contained in these schedules is the responsibility of the department's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1 to the financial schedules, the department's financial schedules are prepared in accordance with state accounting policy. Accordingly, the accompanying financial schedules are not intended to present the financial position and results of operations in conformity with generally accepted accounting principles.

In our opinion, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances of the Department of Highways for the two years ending June 30, 1988 and 1989, in conformity with the basis of accounting described in Note 1.

Respectfully submitted,

A handwritten signature in cursive script, reading "James Gillett".

James Gillett, CPA
Deputy Legislative Auditor

September 30, 1989

DEPARTMENT OF HIGHWAYS
SCHEDULE OF CHANGES IN FUND BALANCES
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1989

	<u>Special Revenue Funds</u>	<u>Debt Service Funds</u>	<u>Internal Service Funds</u>	<u>Expendable Trust Funds</u>
FUND BALANCE: July 1, 1987	<u>\$145,020,407</u>	<u>\$ 7,424,466</u>	<u>\$31,243,846</u>	<u>\$241,011</u>
<u>ADDITIONS:</u>				
<u>Fiscal Year 1987-88</u>				
Budgeted Revenue & Transfers In	164,384,334		15,925,535	
Cash Transfers In	100,059,909 ¹			
Nonbudgeted Revenue & Transfers In		10,700,955		15,610
Nonbudgeted Expenditures & Transfers Out			985,250	
Prior Year Revenue Adjustments	38,081		2,757	
Prior Year Expenditure Adjustments	4,665,207		40,802	
Nonbudgeted Prior Year Expenditure Adjustments			1,360,841	
Direct Entries To Fund Balance	2,883,155	726,001	88,931	
Prior Year Transfer Out Adjustment	8,878			
<u>Fiscal Year 1988-89</u>				
Budgeted Revenue & Transfers In	168,642,103		15,945,903	
Cash Transfers In	100,796,317 ¹			
Prior Year Expenditure Adjustments	198,247			
Prior Year Expenditure/Deduction Adjustment	3,373,752			
Direct Entries To Fund Balance			20,981	
Nonbudgeted Revenue & Transfers In	<u> </u>	<u>10,662,206</u>	<u> </u>	<u>19,796</u>
Total Additions	<u>545,049,983</u>	<u>22,089,162</u>	<u>34,371,000</u>	<u>35,406</u>
<u>REDUCTIONS:</u>				
<u>Fiscal Year 1987-88</u>				
Budgeted Expenditures & Transfers Out	257,082,901		16,314,388	
Prior Year Transfer In Adjustment			8,878	
Nonbudgeted Expenditures & Transfers Out		8,126,897		9,243
<u>Fiscal Year 1988-89</u>				
Budgeted Expenditures & Transfers Out	269,033,633		16,567,426	
Prior Year Revenue Adjustments	69,930		5,862	
Nonbudgeted Expenditures & Transfers Out		10,643,928	(1,205,458)	33,190
Prior Year Expenditure Adjustments			28,380	
Nonbudgeted Prior Year Expenditure Adjustment			(1,724,990)	
Direct Entries To Fund Balance	<u>21,254</u>	<u> </u>	<u> </u>	<u> </u>
Total Reductions	<u>526,207,718</u>	<u>18,770,825</u>	<u>29,994,486</u>	<u>42,433</u>
FUND BALANCE: June 30, 1989	<u>\$163,862,672</u>	<u>\$10,742,803</u>	<u>\$35,620,360</u>	<u>\$233,984</u>

¹ See footnote 6 on page 20.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 18 through 21.

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DEPARTMENT OF HIGHWAYS
SCHEDULE OF BUDGETED REVENUE & TRANSFERS IN - ESTIMATE & ACTUAL
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1989

	<u>Licenses and Permits</u>	<u>Taxes</u>	<u>Charges For Services</u>	<u>Investment Earnings</u>	<u>Sale of Documents & Merchandise</u>	<u>Rentals, Leases & Royalties</u>	<u>Miscellaneous</u>	<u>Grants, Contracts, Donations</u>	<u>Other Sources</u>	<u>Federal</u>	<u>Total</u>
<u>Fiscal Year 1988-89</u>											
SPECIAL REVENUE FUNDS											
Estimated Revenue	\$15,373,100	\$8,132,000	\$15,140,110	\$7,098,496	\$470,260	\$105,000	\$225,000	\$ 353,331	\$25,137,194	\$ 96,207,583	\$168,242,074
Actual Revenue	<u>16,197,170</u>	<u>8,773,123</u>	<u>13,405,269</u>	<u>6,219,266</u>	<u>379,569</u>	<u>103,582</u>	<u>254,778</u>	<u>59,174</u>	<u>18,934,905</u>	<u>104,315,267</u>	<u>168,642,103</u>
Collections Over (Under) Estimate	\$ <u>824,070</u>	\$ <u>641,123</u>	\$ <u>(1,734,841)</u>	\$ <u>(879,230)</u>	\$ <u>(90,691)</u>	\$ <u>(1,418)</u>	\$ <u>29,778</u>	\$ <u>(294,157)</u>	\$ <u>(6,202,289)</u>	\$ <u>8,107,684</u>	\$ <u>400,029</u>
INTERNAL SERVICE FUNDS											
Estimated Revenue			\$14,578,692		\$360,000		\$ 5,500		\$ 1,705,659		\$ 16,649,851
Actual Revenue			<u>14,791,041</u>		<u>350,099</u>		<u>4,763</u>		<u>800,000</u>		<u>15,945,903</u>
Collections Over (Under) Estimate			\$ <u>212,349</u>		\$ <u>(9,901)</u>		\$ <u>(737)</u>		\$ <u>(905,659)</u>		\$ <u>(703,948)</u>
<u>Fiscal Year 1987-88</u>											
SPECIAL REVENUE FUNDS											
Estimated Revenue	\$15,213,686	\$8,297,191	\$14,309,598	\$7,025,000	\$ 60,000	\$105,000	\$300,000	\$ 501,719	\$15,023,916	\$ 98,141,839	\$158,977,949
Actual Revenue	<u>15,699,160</u>	<u>7,965,175</u>	<u>12,960,077</u>	<u>9,064,460</u>	<u>69,943</u>	<u>96,354</u>	<u>345,743</u>	<u>141,757</u>	<u>10,286,872</u>	<u>107,754,793</u>	<u>164,384,334</u>
Collections Over (Under) Estimate	\$ <u>485,474</u>	\$ <u>(332,016)</u>	\$ <u>(1,349,521)</u>	\$ <u>2,039,460</u>	\$ <u>9,943</u>	\$ <u>(8,646)</u>	\$ <u>45,743</u>	\$ <u>(359,962)</u>	\$ <u>(4,737,044)</u>	\$ <u>9,612,954</u>	\$ <u>5,406,385</u>
INTERNAL SERVICE FUNDS											
Estimated Revenue			\$13,997,146		\$330,000		\$ 5,500		\$ 1,930,659		\$ 16,263,305
Actual Revenue			<u>13,702,730</u>		<u>286,635</u>		<u>5,511</u>		<u>1,930,659</u>		<u>15,925,535</u>
Collections Over (Under) Estimate			\$ <u>(294,416)</u>		\$ <u>(43,365)</u>		\$ <u>11</u>		\$ <u>-0-</u>		\$ <u>(337,770)</u>

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 18 through 21.

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DEPARTMENT OF HIGHWAYS
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES AND TRANSFERS OUT
BY OBJECT AND FUND - BUDGET AND ACTUAL
FOR THE FISCAL YEAR ENDED JUNE 30, 1989

	General Operations	Construction	Maintenance	Preconstruction	Highway Service Revolving	State Motor Pool	Equipment	Interfund Transfers	Stores Inventory	G.V.W.	Total
PERSONAL SERVICES											
Salaries	\$ 2,963,216	\$ 13,215,654	\$ 15,345,367	\$ 5,618,177	\$ 1,492,644	\$ 98,644	\$ 2,747,070			\$ 2,178,470	\$ 43,659,242
Other Compensation	5,100										5,100
Employee Benefits	<u>624,641</u>	<u>2,874,484</u>	<u>3,797,671</u>	<u>1,141,630</u>	<u>315,596</u>	<u>25,080</u>	<u>675,458</u>			<u>501,039</u>	<u>9,955,599</u>
Total	<u>3,592,957</u>	<u>16,090,138</u>	<u>19,143,038</u>	<u>6,759,807</u>	<u>1,808,240</u>	<u>123,724</u>	<u>3,422,528</u>			<u>2,679,509</u>	<u>53,619,941</u>
OPERATING EXPENSES											
Contracted Services	1,773,066	124,873,238	1,150,973	5,085,206	459,598	32,839	277,206		\$ 143,480	142,413	133,938,019
Supplies & Materials	216,038	302,248	558,920	89,294	198,962	127,332	2,208,495		2,575,654	43,140	6,320,083
Communications	228,144	305,282	166,787	73,131	22,027	769	9,223		3,246	47,699	856,308
Travel	212,712	1,118,522	81,279	285,472	29,435	318	20,644			69,116	1,817,498
Rent	110,201	1,449,899	8,943,733	2,436	8,827	2,862	1,783		694,999	144,599	11,359,339
Utilities	13,000	18,877	1,476,142		2,293	5,743	38,023		558	50,813	1,605,449
Repair & Maintenance	88,601	127,898	10,553,556	6,272	64,927	40,089	1,776,315		8,492,055	39,674	21,189,387
Other Expenses	<u>30,610</u>	<u>11,824</u>	<u>41,454</u>	<u>26,191</u>	<u>44,784</u>	<u>460</u>	<u>27,396</u>		<u>21</u>	<u>86,418</u>	<u>269,158</u>
Total	<u>2,672,372</u>	<u>128,207,788</u>	<u>22,972,844</u>	<u>5,568,002</u>	<u>830,853</u>	<u>210,412</u>	<u>4,359,085</u>		<u>11,910,013</u>	<u>623,872</u>	<u>177,355,241</u>
EQUIPMENT AND INTANGIBLE											
Equipment	225,979	357,036	73,327	514,231	266,079	567,859	4,977,583			15,460	6,997,554
Intangible Assets		<u>1,829</u>		<u>22,399</u>	<u>1,063</u>						<u>25,291</u>
Total	<u>225,979</u>	<u>358,865</u>	<u>73,327</u>	<u>536,630</u>	<u>267,142</u>	<u>567,859</u>	<u>4,977,583</u>			<u>15,460</u>	<u>7,022,845</u>
CAPITAL OUTLAY											
Land & Interest In Land			54,760	2,851,765							2,906,525
Buildings		<u>592</u>	<u>68,978</u>	<u>2,600</u>						<u>58,171</u>	<u>130,341</u>
Total		<u>592</u>	<u>123,738</u>	<u>2,854,365</u>						<u>58,171</u>	<u>3,036,866</u>
GRANTS											
From State Sources	<u>14,230,126</u>										<u>14,230,126</u>
Total	<u>14,230,126</u>										<u>14,230,126</u>
TRANSFERS											
Accounting Entity Transfers							800,000	\$29,525,390			30,325,390
Total							<u>800,000</u>	<u>29,525,390</u>			<u>30,325,390</u>
DEBT SERVICE											
Bonds	7,584										7,584
Leases		<u>3,069</u>									<u>3,069</u>
Total	<u>7,584</u>	<u>3,069</u>									<u>10,653</u>
TOTAL PROGRAM EXPENDITURES	<u>\$ 20,729,018</u>	<u>\$144,660,452</u>	<u>\$ 42,312,947</u>	<u>\$ 15,718,804</u>	<u>\$ 2,906,235</u>	<u>\$ 901,995</u>	<u>\$ 13,559,196</u>	<u>\$29,525,390</u>	<u>\$11,910,013</u>	<u>\$ 3,377,012</u>	<u>\$285,601,062</u>
SPECIAL REVENUE FUND											
Budgeted	\$ 21,150,218	\$151,155,810	\$ 42,602,877	\$ 16,045,128			\$ 1,705,659	\$37,120,389	\$13,672,810	\$ 3,503,362	\$286,956,253
Actual	<u>20,729,017</u>	<u>144,660,451</u>	<u>42,312,947</u>	<u>15,718,803</u>			<u>800,000</u>	<u>29,525,390</u>	<u>11,910,013</u>	<u>3,377,012</u>	<u>269,033,633</u>
Unspent Budget Authority	<u>\$ 421,201</u>	<u>\$ 6,495,359</u>	<u>\$ 289,930</u>	<u>\$ 326,325</u>			<u>\$ 905,659</u>	<u>\$ 7,594,999</u>	<u>\$ 1,762,797</u>	<u>\$ 126,350</u>	<u>\$ 17,922,620</u>
INTERNAL SERVICE FUNDS											
Budgeted					\$ 2,997,581	\$ 919,871	\$ 12,909,458				\$ 16,826,910
Actual					<u>2,906,235</u>	<u>901,995</u>	<u>12,759,196</u>				<u>16,567,426</u>
Unspent Budget Authority					<u>\$ 91,346</u>	<u>\$ 17,876</u>	<u>\$ 150,262</u>				<u>\$ 259,484</u>

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 18 through 21.

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DEPARTMENT OF HIGHWAYS
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES AND TRANSFERS OUT
BY OBJECT AND FUND - BUDGET AND ACTUAL
FOR THE FISCAL YEAR ENDED JUNE 30, 1988

	General Operations	Construction	Maintenance	Preconstruction	Highway Service Revolving	State Motor Pool	Equipment	Interfund Transfers	Stores Inventory	G.V.W	Total
PERSONAL SERVICES											
Salaries	\$ 2,912,329	\$ 12,920,766	\$14,641,882	\$ 5,389,202	\$1,493,766	\$ 93,071	\$ 2,707,671			\$2,035,205	\$ 42,193,892
Other Compensation	4,281	1,197	856							756	7,090
Employee Benefits	612,521	2,788,640	3,876,646	1,102,710	311,604	25,872	703,199			485,078	9,906,270
Total	3,529,131	15,710,603	18,519,384	6,491,912	1,805,370	118,943	3,410,870			2,521,039	52,107,252
OPERATING EXPENSES											
Contracted Services	1,780,604	124,198,984	1,526,459	3,793,466	480,290	35,791	268,738		\$ 88,646	197,552	132,370,530
Supplies & Materials	210,259	368,090	604,693	77,571	212,041	139,891	2,014,698		2,304,552	44,383	5,976,178
Communications	210,532	260,199	146,234	79,934	23,452	856	15,663		4,238	44,080	785,188
Travel	203,308	1,144,201	102,129	268,723	28,063	180	27,267			101,367	1,875,238
Rent	97,730	1,362,113	7,939,823	1,734	5,741	2,699	12,972		731,589	135,867	10,290,268
Utilities	15,251	18,731	1,360,651		1,991	4,772	33,575		984	42,831	1,478,786
Repair & Maintenance	91,624	171,224	10,639,055	4,740	54,039	45,066	1,498,438		9,113,642	71,934	21,689,762
Other Expenses	24,220	20,134	40,615	10,934	49,904	340	33,256		725	79,968	260,096
Total	2,633,528	127,543,676	22,359,659	4,237,102	855,521	229,595	3,904,607		12,244,376	717,982	174,726,046
EQUIPMENT AND INTANGIBLE ASSETS											
Equipment	277,029	195,217	99,438	351,031	131,842	408,375	5,447,208			53,504	6,963,644
Intangible Assets		650			2,057						2,707
Total	277,029	195,867	99,438	351,031	133,899	408,375	5,447,208			53,504	6,966,351
CAPITAL OUTLAY											
Land & Interest In Land			7,388	2,343,967							2,351,355
Buildings			9,042							99,855	108,897
Other Improvements										135	135
Total			16,430	2,343,967						99,990	2,460,387
GRANTS											
From State Sources	14,236,434										14,236,434
Total	14,236,434										14,236,434
TRANSFERS											
Accounting Entity Transfers							1,930,659	\$20,924,040			22,854,699
Total							1,930,659	20,924,040			22,854,699
DEBT SERVICE											
Bonds	46,120										46,120
Total	46,120										46,120
TOTAL PROGRAM EXPENDITURES	\$20,722,242	\$143,450,146	\$40,994,911	\$13,424,012	\$2,794,790	\$756,913	\$14,693,344	\$20,924,040	\$12,244,376	\$3,392,515	\$273,397,289
SPECIAL REVENUE FUND											
Budgeted	\$21,089,889	\$168,884,329	\$41,251,535	\$19,570,289			\$ 1,930,659	\$25,661,084	\$13,202,298	\$3,497,307	\$295,087,390
Actual	20,722,242	143,450,146	40,994,911	13,424,012			1,930,659	20,924,040	12,244,376	3,392,515	257,082,901
Unspent Budget Authority	\$ 367,647	\$ 25,434,183	\$ 256,624	\$ 6,146,277			\$ 0	\$ 4,737,044	\$ 957,922	\$ 104,792	\$ 38,004,489
INTERNAL SERVICE FUNDS											
Budgeted					\$2,998,157	\$759,377	\$12,835,627				\$ 16,593,161
Actual					2,794,790	756,913	12,762,685				16,314,388
Unspent Budget Authority					\$ 203,367	\$ 2,464	\$ 72,942				\$ 278,773

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 18 through 21.

DEPARTMENT OF HIGHWAYS
NOTES TO THE FINANCIAL SCHEDULES
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1989

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Department of Highways operated under a director appointed by the Governor and consisted of the following programs during the audit period: General Operations, Construction, Maintenance, Preconstruction, Highway Service Revolving, State Motor Pool, Equipment, Interfund Transfers, Stores Inventory, Bonds, and Gross Vehicle Weight.

The following is a summary of the significant accounting policies:

Basis of Presentation

The financial schedules are prepared from the Statewide Budgeting and Accounting System without adjustments. Accounts are organized on the basis of funds according to state law. The following fund types are used by the department:

Special Revenue Fund - accounts for the proceeds of specific revenue sources that are legally restricted to expenditures for specific purposes. Legislative appropriation is required to spend from this fund. Department Special Revenue Funds include the Highway Revenue Bond Proceeds Account, the Reconstruction Trust Account, the Bond Construction Accounts, the Highway Special Revenue Account, and the Highway Trust Account. The Highway Trust Account reflects receipts and expenditures of federal moneys designated for highway construction.

Debt Service Fund - accounts for the accumulation of resources for the payment of General Long-term Debt Principal and Interest. This fund accounted for payments relating to the department's series 1987 Revenue Bonds (\$150,000,000), which was used to defease previous revenue bond and bond anticipation notes and generate additional construction money. Payments for the Highway Building Complex Bonds were also accounted for in this fund.

Internal Service Fund - accounts for operations that provide goods or services to other agencies or departments on a cost-reimbursement basis. At the Department of Highways the Internal Service Fund includes the Motor Pool, Highway Service, and Equipment Bureau Revolving Accounts.

Expendable Trust Fund - accounts for assets held by the department in a trustee capacity where both the trust principal and earnings may be expended. The department accounts for the Woodville Highway Account in this fund. The account reflects the proceeds and interest earned on the sale of a section of highway to the Anaconda Company. The department is holding these moneys in trust with the intent that they be used to improve Butte-Silver Bow area roadways.

Basis of Accounting

The state of Montana uses the modified accrual basis of accounting, described in the Montana Operations Manual, to account for the Special Revenue, Debt Service, and Expendable Trust Funds.

Under the modified accrual basis of accounting, expenditures are recorded for valid obligations. A valid obligation exists when the associated liability is incurred and includes the following items which are also considered valid obligations under state accounting policy.

- If the appropriation provided funds to complete a given project, the entire amount of a service contract may be accrued even though the services are rendered in a fiscal year subsequent to the fiscal year in which the expenditure is accrued.
- Equipment expenditures may be accrued in the fiscal year in which a purchase order was issued.
- Goods ordered, but not received as of the fiscal year-end, may be accrued if the purchase order was issued in the fiscal year in which the anticipated expenditure is to be accrued.

Revenues are recorded when they are received in cash, unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available to finance expenditures of the current fiscal period.

The department uses the full accrual basis of accounting for the Internal Service Funds. Under this basis, revenue is recognized when earned. Expenses are recognized when a valid obligation, as defined above, is incurred.

2. VACATION AND SICK LEAVE

Employees of the department accumulate both vacation and sick leave. Employees are paid for 100 percent of unused vacation and 25 percent of unused sick leave credits upon termination. Accumulated unpaid liabilities for vacation and sick leave are not reflected in the financial schedules of the department. Expenditures for termination pay currently are absorbed in the annual operational costs of the department. At June 30, 1989, the department had an estimated liability of \$6,955,958 for vacation and sick leave.

3. PENSION PLAN

Employees are covered by the Montana Public Employees' Retirement System (PERS). The department's contributions to this plan were \$2,703,719 in fiscal year 1987-88 and \$2,793,356 in fiscal year 1988-89.

4. BOND ACTIVITY

The department has issued bonds on several occasions since 1983. The bond issues fund the Highway Reconstruction Trust and the accelerated interstate projects. The department issued \$150,000,000 in bonds in April 1987. The April issue was used to defease a June 1983 issue and a July 1985 issue and generate additional operating cash.

Bond activity was primarily recorded in the debt service fund. The activity in the debt service fund was nonbudgeted activity.

Nonbudgeted Revenue and Transfers In by Class

Fiscal Year	<u>Investment Earnings</u>	<u>Transfers In</u>	<u>Total</u>
1987-88	\$ 63,787	\$10,637,168	\$10,700,955
1988-89	\$ 71,721	\$10,590,485	\$10,662,206

Nonbudgeted Expenditures and Transfers Out by Program

Fiscal Year	<u>Bonds</u>	<u>Totals</u>
1987-88	\$ 8,126,897	\$ 8,126,897
1988-89	\$10,643,928	\$10,643,928

5. INTRAFUND TRANSFERS

The department uses transfer activity to move cash to appropriate accounts to make payments to vendors, meet reserve requirements on debt or make payments on bonds. Some of these transfer transactions were between accounts within the same fund. These transfers occurred within the Special Revenue Fund and amounted to \$10,286,872 and \$18,934,905 in fiscal years 1987-88 and 1988-89, respectively.

6. CASH TRANSFERS

The department receives gasoline and diesel fuel tax receipts as a source of funding. This money is collected by the Department of Revenue and recorded as revenue to the state at the time of collection. To avoid duplicate recording of the same revenue on the state's accounting records, the state's accounting system

deposits the cash in a Department of Highways account. These cash transfers are shown on the Schedule of Changes in Fund Balance for the two years ended June 30, 1989 on page 14.

7. ADVANCED CONSTRUCTION INTERSTATE

Federal interstate funds are matched by state funds. The ACI (Advanced Construction Interstate) program was designed to allow the department to accelerate the construction of interstate by committing future federal interstate funds for current construction activities. This enables the state to complete sections of interstate at one time, gaining the engineering and economic benefits of economy of scale and avoiding future inflation costs. The ACI program was tied to the issuance of bonds for immediate highway construction, with the bonds being repaid as additional federal funds are committed to interstate highway projects.

The department had expended \$38,635,428 of the bond funds dedicated to ACI as of June 30, 1988 and an additional \$621,757 was expended during fiscal year 1988-89 on ACI projects. Of the \$38,456,834 of bond funds used, \$38,450,916 have been reimbursed by the federal government as of June 30, 1989. The remaining costs have been paid by the state.

8. COMMITMENTS

Construction commitments in the form of unperformed contracts for the construction of highways existed at the department at the end of fiscal years 1987-88 and 1988-89. The authorized, expended and unexpended amounts are presented, in the following schedule, by district.

	<u>Project Authorization</u>	<u>Expended through June 30</u>	<u>Remaining Construction Authorization</u>
<u>Fiscal Year 1987-88</u>			
Billings District	\$ 39,757,562	\$ 21,401,619	\$18,355,943
Butte District	25,969,036	13,569,702	12,399,334
Missoula District	41,048,893	17,519,797	23,529,096
Great Falls District	34,700,845	19,745,271	14,955,574
Glendive District	36,273,537	29,155,966	7,117,571
Total Highways	<u>\$177,749,873</u>	<u>\$101,392,355</u>	<u>\$76,357,518</u>
<u>Fiscal Year 1988-89</u>			
Billings District	\$ 23,743,905	\$ 16,403,835	\$ 7,340,070
Butte District	28,836,072	19,872,729	8,963,343
Missoula District	56,966,865	30,352,262	26,614,603
Great Falls District	30,025,654	22,034,860	7,990,794
Glendive District	32,583,471	20,624,826	11,958,645
Total Highways	<u>\$172,155,967</u>	<u>\$109,288,512</u>	<u>\$62,867,455</u>

AGENCY RESPONSE

DEPARTMENT OF HIGHWAYS



STAN STEPHENS, GOVERNOR

2701 PROSPECT AVE.

STATE OF MONTANA

HELENA, MONTANA 59620

December 1, 1989

Received

DEC 1 1989

Montana Legislative Audit

Scott A. Seacat
Legislative Auditor
Room 135
State Capitol
Helena, MT 59620

Subject: Department of Highways' Financial Compliance Audit
for Fiscal Years 1987-88 and 1988-89

I am transmitting our response performed by your office for the two
fiscal years ended June 30, 1989.

Thank you for your staff's effort and cooperation during this audit.

If you have questions concerning our response, please call me at
444-6201.

A handwritten signature in cursive script, reading "Larry W. Larsen".

Larry W. Larsen, P.E.
Director of Highways

LWL:WGS:dak:4ii

Recommendation #1

We recommend the department:

- A. Implement policies requiring review and approval of project estimates and equipment usage reports; and
- B. Implement procedures to ensure all equipment usage charged to federal projects is adequately supported.

Response:

- A. We concur. As the auditors noted, the department implemented a new personal computer based project estimate system in 1987. The department's training regarding the internal control procedure discussed by the auditor's apparently was not adequate due to the complexity of the change. We have implemented several actions to correct this situation. We have redesigned the project estimate to require a signature on the completed report certifying the project manager has reviewed the completed project estimate form and the quantities submitted were accurately processed. The Construction Bureau issued a memorandum on November 28, 1989 explaining the new form and established this procedure as a formal policy. The revised construction manual will also include this procedure and the department will review project estimates in the field by several district and headquarters personnel to assure compliance.
- B. We concur. The Equipment Bureau redesigned the equipment usage reports after the auditors notified us of the deficiency. This report requires a review and approval signature. The Accounting and Equipment Manuals also state the proper policy and procedure. We will emphasize this requirement during additional field training.

We are also examining alternative methods to recover these costs from the federal government to replace this extensive process.

Recommendation #2

We recommend the department implement procedures to ensure disposal of scrap metal and recording of related revenue and expenditures are in compliance with State law and policy.

Response:

We concur.

Recommendation #3

We recommend the department encourage periodic meetings among the District Centralized Services Supervisors.

Response:

We concur. We will schedule regular meetings rotated between the five districts with participation and direction from the Helena Headquarters Centralized Services Division.

WGS:dak:4ii/3

